



Economic Update

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Economic Growth Surges in the First Quarter

Overview

Economic growth in the first quarter of 2006 was the fastest in 2½ years, and more than double the rate in the previous quarter. Nevertheless, most analysts project a return to more moderate – though still healthy – growth over the remainder of the year.

Sustained job growth across most sectors contributed to low unemployment throughout the first quarter. Personal incomes and expenditures also showed strong gains in April. Energy prices spiked after the middle of the month, but have backed off from their high point due to growth in gasoline inventories.

Analysts are watching for signs of higher energy prices feeding through to the general price level, but so far there is little evidence that this has occurred.

Highlights

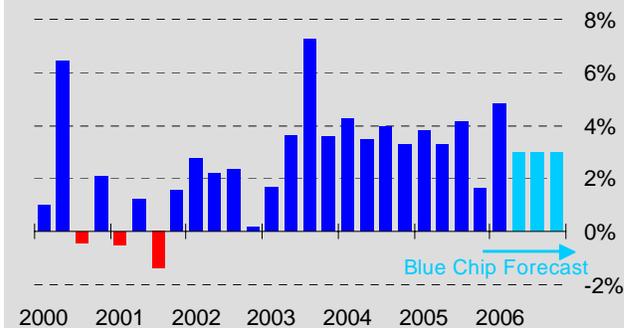
- Gross domestic product [GDP] grew by 4.8 percent in the first quarter of 2006, rebounding from 1.7-percent annualized growth at the end of last year (Fig 1).
- The strong labor market continued in April, as 138,000 jobs were created and the unemployment rate remained at 4.7 percent. The number of new jobs was less than the increases of the prior two months – about 200,000 new jobs each month – but only slightly below the average of 165,000 new jobs created during the past 32 consecutive months of job gains.
- April personal income and consumption expenditures grew by 0.5 percent and 0.2 percent, respectively.
- Business owners experienced greater price inflation, but rising productivity in part shielded consumer purchase prices from wage and energy cost increases.

First-Quarter Growth

The 4.8-percent first-quarter growth in GDP – a broad measure of the Nation’s output of goods and services – was driven by positive contributions from consumption expenditures (5.5 percent), equipment and software (16.4 percent), exports (12.1 percent), and Federal Government spending (10.8 percent). Gross domestic product has grown

Economic Growth Since 2000

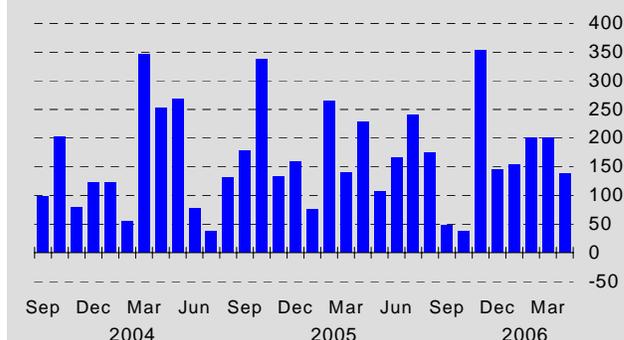
(Real annualized GDP growth rate in each quarter)



Sources: Bureau of Economic Analysis

Close to 5.3 Million Jobs in Past 32 Months

(Change in employment, in thousands)



Source: Bureau of Labor Statistics

(continued on reverse side)

for 18 consecutive quarters, averaging a healthy 3.2 percent (see Fig. 1). The *Blue Chip* forecast – a monthly consensus of private forecasters – is for real GDP growth to return toward healthy trend-like rates of between 3.4 percent and 2.8 percent during the remaining quarters of this year (see Table alongside).

Jobs Growth Continues to Impress

As noted, 138,000-jobs growth in April’s nonfarm payroll employment represents the 32nd consecutive month with job gains (Fig. 2). More than 5.2 million new jobs have been added to payrolls in that period, and around 2.0 million new jobs have been created in the past year alone.

The job growth figure was a decline from the prior two months, during which employment increased in the 200,000-job range each month. Such variations are consistent, however, with the “sawtooth” nature of monthly job-increase figures (see Fig 2). April’s job growth was only slightly lower than the average monthly increase of 165,000 jobs during the past 32 months.

The unemployment rate, based on a survey of households, held steady at 4.7 percent in April, remaining below the averages of the 1960s, 1970s, 1980s, and 1990s. The unemployment rate has fallen by 1.6 percentage points since its recent peak of 6.3 percent in June 2003.

Energy Prices

Crude oil futures briefly topped \$75 per barrel in the third week of April, but have since retreated, while the national average price of gasoline has reached a plateau of sorts at \$2.90, its highest dollar-value level since September. (In inflation-adjusted terms oil and gas prices are below their 1980 peaks). Factors such as refinery capacity constraints and political uncertainty in Iran – termed “supply-side determinants” – have been blamed for most of the price volatility. There are also indications of declining usage of oil and gasoline, which could relieve some of the pressure behind prices.

Price Inflation

Despite the energy price surge, the overall Consumer Price Index [CPI] – the most common measure of inflation, increased by a relatively moderate 3.4 percent compared to April of last year. Core CPI inflation (which excludes inflation in energy and food prices) was up 2.1 percent compared to a year ago. Analysts and the Federal Reserve

	2005				2006			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	<i>Actual</i>				<i>Projected</i>			
Real GDP Growth	3.8	3.3	4.1	1.7	4.8	3.4	3.0	2.8
Unemployment Rate	5.3	5.1	5.0	4.9	4.7	4.7	4.7	4.7
CPI Inflation	2.3	3.8	5.5	3.3	2.2	3.2	2.4	2.4
3-month Treas. Bill	2.5	2.9	3.4	3.8	4.4	4.8	5.0	4.9
10-year Treas. Note	4.3	4.2	4.2	4.5	4.6	5.0	5.1	5.2

are watchful of whether higher energy prices will begin to pass through to the core inflation measure in areas such as transportation costs and the prices of manufacturing inputs.

Federal Reserve Policy

With robust economic growth and risks of energy price increases leading to higher general inflation, the Federal Reserve, at its May 10 policymaking meeting, continued its recent course of monetary policy by increasing its target for overnight interest rates again by a quarter percent, to 5.0 percent. The Fed has raised overnight rates in a sequence of 16 quarter-point hikes that began in June 2004, bringing the overnight rate from 1.00 percent to the current 5.00 percent.

Market guesses about whether the Fed will institute another quarter-point increase at the next meeting, scheduled for June 28 and 29, have been variable and “data dependent.” Currently, Federal funds futures prices can be interpreted as projecting a pause through August.

Upcoming Indicators

Inflation - The Consumer Price Index for April is scheduled to be released on *May 17*.

GDP - A revised estimate of GDP growth for the 1st quarter of 2006 is scheduled for release on *May 25*.

Employment - May employment and unemployment data are scheduled for release on *June 2*.

Federal Reserve - The Fed’s next monetary policy meeting is scheduled for *June 28 and 29*.

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